UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF MONTANA

In re **ERNEST R NUNN**, and **CAROLYN J NUNN**, Debtors.	Case No. **05-60354-13**

MEMORANDUM of DECISION

At Butte in said District this 20th day of January, 2006.

In this Chapter 13 bankruptcy, after due notice, a hearing was held January 10, 2006, in Butte on: (1) Debtors' "Motion for Approval of Distribution of Proceeds from Sale of 8 Acres" (Dkt. 117) filed December 1, 2005, as superseded by Debtors' "Amended Motion for Approval of Distribution of Proceeds from Sale of 8 Acres" filed December 29, 2005 (Dkt. 150), together with the consents thereto filed by Mountain West Bank on December 5, 2005 (Dkt. 120), and January 4, 2006 (Dkt. 157), and the Small Business Administration on December 20, 2005 (Dkt. 131), and the objections thereto filed by Wells Fargo Bank, N.A. on December 11, 2005 (Dkt. 124),[1] and January 9, 2006 (Dkt. 169), and the Chapter 13 Trustee on December 29, 2005 (Dkt.

[1] Mountain West Bank filed a "Response to Wells Fargo Objection to Nunn Motion for Distribution of Proceeds of Sale of 8 Acre Lot" on December 15, 2005, at docket entry 126. Additionally, the Small Business Administration filed a "Response to Wells Fargo Objection to Distribution" on December 19, 2005, at docket entry 131 and Debtors filed a "Response to Wells Fargo's Objection to Motion for Approval of Distribution of Proceeds from Sale of 8 Acres" on December 20, 2005, at docket entries 135 and 141.

147); and (2) the "Motion to Approve Sale of Silos Inn Held December 15, 2005" (Dkt. 130) filed by attorney Lewis K. Smith on behalf of Debtors on December 20, 2005, together with the objections thereto filed by attorney Gregory W. Duncan on behalf of Debtors (Dkt. 137 and 140), Mountain West Bank (Dkt.142) on December 22, 2005, and the Chapter 13 Trustee on December 29, 2005 (Dkt. 148), and the "Response Supporting Motion to Approve Sale of Silos" filed by Gateway Economic Development Corporation on December 30, 2005 (Dkt. 156), and the "Response Supporting Motion to Approve Sale of Silos" filed by Lewis Reeves on January 5, 2006 (Dkt. 161). The Chapter 13 Trustee, Robert G. Drummond, appeared at the hearing; Debtors were represented by Gregory W. Duncan and Lewis K. Smith; Mountain West Bank was represented by Jonathan Motl; Gateway Economic Development Corporation was represented by Dale Reagor; Wells Fargo Bank, N.A. was represented by John Grant; Lewis Reeves was represented by James Screnar; and the Small Business Administration was represented by Michael Bayuk. The Court heard testimony from attorney Lewis K. Smith, debtor Ernest Nunn, James Campbell and Robin Notnagle. Debtors Exhibits 1 through 6, Mountain West Bank's Exhibit A, and Wells Fargo Bank, N.A.'s Exhibits 1 and 2 were admitted into evidence without objection. At the conclusion of the hearing, the Court took both matters under advisement. This Memorandum of Decision sets forth the Court's findings of fact and conclusions of law.

I. Motion for Approval of Distribution of Proceeds from Sale of 8 Acres.

On September 14, 2005, Debtors filed a Motion to Sell seeking to sell an 8 acre parcel of land. Debtors' Motion to Sell did not disclose the sales price of the property and was not accompanied by a copy of the Buy/Sell agreement. The foregoing Motion was superseded by a

Motion for Approval of Buy/Sell on 8 Acre Lot filed by Debtors on September 21, 2005. In the Motion filed September 21, 2005, Debtors sought approval to sell the 8 acre parcel of land for the sum of $115,000. Debtors' also identify the Small Business Administration, Mountain West Bank and all unsecured creditors as having a current interest in the 8 acre parcel of land. Mountain West Bank filed a consent to Debtors' September 21, 2005, Motion on September 22, 2005. After the Court received no objection to Debtors' Motion, the Court entered an order on October 5, 2005, granting Debtors' Motion for Approval of Buy/Sell of 8 Acre Lot "free and clear of all liens . . . for the sum of $115,000 in accordance with the (Land) Buy-Sell Agreement attached to their Motion, with all valid liens attaching to the proceeds of the sale."

Approval of the sale was followed by Debtors' Motion for Approval of Distribution of Proceeds wherein Debtors acknowledge that Wells Fargo Bank has a first security interest in the 8 acre parcel of land. However, Debtors seek to pay from the sales proceeds, after payment of a real estate commission and closing costs, the Small Business Administration ($26,363.83), Mountain West Bank ($73,000 by agreement), the arrearage owing to Wells Fargo Bank ($8,433.05 consisting of 4 delinquent payments totaling $6,720.72, late charges of $122.93 and bankruptcy fees and costs of $1,589.40) and property taxes owed to Broadwater County ($466.52). Debtors seek to distribute the funds as set forth above arguing that Wells Fargo Bank is also secured by Debtors' family dwelling that is located on a separate and distinct 5 acre parcel of land. Debtors' assert that the value of their home is at least $240,000 pursuant to an appraisal done in 1999, and because Wells Fargo Bank is only owed $161,603.25,[2] it is

[2] The figure of $161,603.25 comports with Proof of Claim No. 4 filed by Wells Fargo Bank on March 15, 2005. Wells Fargo Bank's claim is secured by a Deed of Trust that

oversecured and adequately protected. A statement was made at the hearing that the Small Business Administration and Mountain West Bank are not secured by other properties. To the contrary, Mountain West Bank, in a response to a Motion to Avoid Lien filed by Debtors, recites that Mountain West Bank has a consensual lien on the 5 acre parcel of land that includes Debtors' residence.

Wells Fargo Bank did not oppose Debtors' sale of the property. However, Wells Fargo Bank strongly opposes Debtors' proposed distribution arguing: (1) it has an allowed claim under 11 U.S.C. § 502; (2) that it bargained for a first lien position on 13 acres of land, not 5; (3) that the buy-sell provided that all liens on the property would be paid in full; (4) that the sale of the 8 acres free and clear of liens is not permitted under any of the 5 grounds set forth in 11 U.S.C. § 363(f); (5) if the sales proceeds are not sufficient to pay all secured claims, the subordinate liens should be shorted, not the first lien holder; (6) Debtors' proposed distribution ignores the due on sale clause set forth in the Deed of Trust; (7) that Debtors' proposed Chapter 13 plan contemplates no payments to Wells Fargo Bank until Debtors' home is sold; (8) Debtors' 1999 appraisal of the home is stale; (9) sale of the property prior to confirmation violates 11 U.S.C. § 1306(b); (10) that the sale is nothing more that a *de facto* reorganization where the sale masquerades as a plan and thereby defeats the protections afforded to creditors by the Bankruptcy Code.

There is no dispute among the parties that Wells Fargo Bank has an allowed secured

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encompasses 2 separately described parcels of land; the 5 acre parcel on which the family home is located and the 8 acre parcel that has been sold. Debtors have not objected to Wells Fargo Bank's Proof of Claim and the claim is thus deemed allowed under 11 U.S.C. § 502.

claim under 11 U.S.C. § 502. In addition, Wells Fargo Bank's arguments identified as 3, 4, 9 and 10 above are simply not timely. Wells Fargo Bank had the opportunity to object to Debtors' Motion for Approval of Buy/Sell on 8 Acre Lot filed September 21, 2005, and did not. Consequently, the Court approved the sale without objection on October 5, 2005. Finally, argument 7 addresses confirmation of Debtors' Chapter 13 plan, which matter is not now before the Court.

The Court agrees that Debtors' valuation figure of $240,000 based upon a 1999 appraisal is stale.[3] However, Mountain West Bank had an appraisal of Debtors' residence, located on 5 acres, done as of December 27, 2005, and as of that date, Debtors' home was valued by James R. Campbell at $260,000. The appraisal done by James R. Campbell as of December 27, 2005, was the most persuasive evidence of value presented at the hearing and thus, the Court sets the value of Debtors' residence for purposes of this case at $260,000. The December 27, 2005, appraisal and valuation renders Wells Fargo Bank's 8th objection to Debtors' Motion moot.

The Court agrees with Wells Fargo Bank that it undoubtedly bargained for a first lien position on Debtors' entire 13 acres of land, not just the home and 5 acres. The Court also concurs that Debtors' proposed distribution does not provide for any meaningful distribution to Wells Fargo Bank, other than the $8,433.05 delinquency. The Court is also troubled by the fact that Debtors' Motion for Approval of Buy/Sell on 8 Acre Lot does not identify Wells Fargo Bank as having a first lien position on the property nor does Debtors' Motion identify all creditors with liens against the property. As noted earlier, Debtors' September 21, 2005, Motion

[3] This Court has long adhered to the presumption that any sale or valuation occurring more than one-year prior to a valuation determination is stale and thus, is not persuasive evidence for the purposes of establishing the current market value for real property .

merely identifies the Small Business Administration and Mountain West Bank as having an interest in the 8 acre parcel of land. The Title Report prepared by Stewart Title Guaranty Company dated October 10, 2005, reflects that the following entities have an interest in the 8 acre parcel of land:

Deed of Trust dated March 25, 1999, to Wells Fargo Bank

Montana Trust Indenture dated November 20, 2000, to the Small Business Administration

Judgment filed July 2, 2003, by Commtech Services, Inc.

Judgment filed January 9, 2004, by Mountain West Bank[4]

Judgment filed February 17, 2004, by Montana Nursing Association

Judgment filed April 16, 2004, by U.S. Bank

Supplemental Judgment filed December 17, 2004, by Mountain West Bank

Judgment filed January 6, 2005, by Centron Services, Inc.

Federal Tax Lien

Delinquent Property taxes for 2004 and presumably for 2005.

On December 29, 2005, Debtors filed a Motion to Avoid Lien Under 11 U.S.C. § 522(f), seeking to avoid the judicial liens of Commtech Services, Inc., Mountain West Bank, Montana Nursing Association, U.S. Bank, Centron Services and the federal tax lien. Debtors' seek to avoid the liens held by the above entities against both the 8 acre parcel of land and the 5 acre parcel upon which Debtors' home is situated. Debtors' Motion to Avoid Lien is opposed by

[4] The attachments to Mountain West Bank's Proof of Claim No. 16 filed May 20, 2005, reflect that Debtors executed a Deed of Trust in favor of Mountain West Bank in May of 2002. The Deed of Trust appears to reference Debtors' residence and the 5 acre tract of land.

Mountain West Bank and Commtech Services, Inc. Hearing on Debtors' Motion to Avoid Lien is not scheduled until February 7, 2005, but it would seem from the facts now before the Court that Debtors cannot claim the 8 acre parcel as necessary for their homestead, particularly in light of the fact that Debtors' have voluntarily elected to sell the 8 acre parcel. Moreover, Debtors are not allowed to avoid consensual liens, such as that held by Mountain West Bank, and Debtors are not allowed to avoid statutory liens, such as the federal tax lien. Debtors may, nonetheless, be successful in avoiding any judgment liens that Commtech Services, Inc., Mountain West Bank, the Montana Nursing Association and Centron Services have against Debtors' 5 acre parcel of real property, to the extent that Debtors can establish that the property is indeed their homestead and to the extent that Debtors can show that said homestead exemption is impaired.

At the hearing, the parties indicated that this case involved the marshaling of assets. With respect to the marshaling of assets, Mont. Code Ann. § 31-2-105 provides:

> **Relative rights of different creditors.** Where a creditor is entitled to resort to each of several funds for the satisfaction of his claim and another person has an interest in or is entitled as a creditor to resort to some but not all of them, the latter may require the former to seek satisfaction from those funds to which the latter has no such claim, so far as it can be done without impairing the right of the former to complete satisfaction and without doing injustice to third persons.

This Court addressed the doctrine of marshaling *In re Murdock*, 134 B.R. 417, 422, 10 Mont. B.R. 178, 182-185 (Bankr. Mont. 1991):

> In an exhaustive analysis of the doctrine of marshaling, *In re Vermont Toy Works, Inc*., 82 B.R. 258, 290 (Bankr.Vt.1987), applying Vermont law holds:
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> > Before a Court invokes the equitable doctrine of marshaling, either the funds on which marshaling may be impressed, or all of the parties must be subject to the Court's jurisdiction:
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> > > And in marshaling [sic] assets strictly, it is always regarded as

> indispensable that all the parties in interest should be before the court, so that the decree shall be final and conclusive upon their rights; or at the very least, that the fund should be so before the court that the judgment might operate in rem. *Shedd & Co. v. Bank of Brattleboro*, 32 Vt. 709, 717 (1860).
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> Bankruptcy Courts are courts of equity. They are the gatekeepers of the fair allocation of assets to creditors. As such, when faced with facts which demand a remedy for inequitable conduct they have fashioned various exceptions to marshaling's technical requirements of two or more funds, one of which would otherwise be considered a non-asset asset.
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> Montana Code Annotated section 31-2-105 provides:
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> **Relative rights of different creditors.** Where a creditor is entitled to resort to each of several funds for the satisfaction of his claim and another person has an interest in or is entitled as a creditor to resort to some but not all of them, the latter may require the former to seek satisfaction from those funds to which the latter has no such claim, so far as it can be done without impairing the right of the former to complete satisfaction and without doing injustice to third persons.

See, also, Witbart v. Witbart, 204 Mont. 446, 666 P.2d 1217 (1983), applying such code provision without discussion of marshaling principles.

In *Owens-Corning Fiberglass Corp. v. Center Wholesale, Inc., et al.* (*In re Center Wholesale, Inc.*), 759 F.2d 1440 (9th Cir.1985), the Court, addressing an identical marshaling statute of California, held, following *Duck v. Wells Fargo Bank* (*In re Spectra Prism Industries*), 28 B.R. 397 (9th Cir. BAP 1983), as follows:

> Because the validity, nature, and effect of liens are governed by the law of the state where the property is located, and because California law after *Shedoudy* [*v. Beverly Surgical Supply Company*, 100 Cal.App.3d 730, 161 Cal.Rptr. 164 (1980)] gives judicial lien creditors, such as the debtor in possession under § 544, the power to block a marshaling order, we hold as a matter of law that Center has standing to block Owens-Corning's request for marshaling.

In a second decision involving *Center Wholesale, Inc.*, the Ninth Circuit Court of Appeals further explained the doctrine of marshaling in *In re Center Wholesale, Inc. (II)*, 788 F.2d 541, 544 (9th Cir.1986) as follows:

> Finally, Center's interpretation of our decision would constitute a silent departure from existing law. We have found no authority for the proposition that a trustee or debtor in possession may *require* a senior lienor to satisfy its claim out of a junior lien's collateral. To the contrary, the cases upon which we relied in our prior opinion indicate the opposite result. *See In re Spectra Prism Industries, Inc*., 28 B.R. 397, 399 (9th Cir. BAP 1983) (imposition of marshaling must avoid injustice to third persons, such as other lien creditors); *Shedoudy v. Beverly Surgical Supply Co.*, 100 Cal.App.3d 730, 734, 161 Cal.Rptr. 164, 166 (1980) (marshaling is never applied when the result would be inequitable). If we had intended so radical a departure from existing law, we would have stated our intentions far more clearly. We agree with the reading given our prior opinion by the author of Note, *Marshaling Assets in Bankruptcy: Recent Innovations in the Doctrine*, 6 Cardozo L.Rev. 671, 688 (1985), that
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> > Marshaling prevents a senior secured party from willfully choosing the double-encumbered fund to the prejudice of junior secured parties. If the senior secured party does not choose the double-encumbered fund, however, there is not reason to think that a bankruptcy court would force the senior secured party to act detrimentally to the junior secured party. If the Ninth circuit has destroyed marshaling, it has not invented a new doctrine of "reverse marshaling."

Spectra Prism, *supra*, explains and defines the elements of marshaling under section 31-2-105, to-wit:

> Marshaling [sic] is an equitable doctrine developed historically and traditionally used to prevent a junior lienholder with a security interest in a single property from being squeezed out by a senior lienholder with a security interest not only in that property, but in one or more additional properties. The doctrine requires the senior lienholder to first resort to assets free of the junior lien to avoid the inequity which would otherwise result from the unnecessary elimination of the junior lienholder's security with the increased likelihood the junior creditor will be unable to satisfy its claim.

Shedoudy v. Beverly Surgical Supply Co., 100 Cal.App.3d 730, 733, 161 Cal.Rptr. 164 (1980). The basis for marshaling [sic] is in California Civil Code §§ 2899 and 3433.

There are four basic requirements which must be met before a marshaling order

> may be imposed on a second lienholder. First, there must be two or more funds. Second, only one of the creditors may have the right to resort to both funds. Third, there must be an absence of prejudice to the senior lienholder. Finally, the imposition of marshaling must avoid injustice to third persons. *Victor Gruen Associates v. Glass*, 338 F.2d 826, 829 (9th Cir.1964).

See also, In re Frazier, 17 Mont. B.R. 244, 257-60 (Bankr. D. Mont. 1998) (*quoting* the *In re Murdock, supra*) and *see e.g., In re Kerbs*, 207 B.R. 211, 215 (Bankr. Mont. 1997).

In the instant case, there is basically one fund (with proceeds of something less than $115,000) and one parcel of property (valued at $260,000). As discussed earlier, it appears that all creditors, with the possible exception of the Small Business Administration, have an interest in the funds from the sale of the 8 acre parcel and the right to resort to Debtors' remaining 5 acre parcel of property. However, the judicial liens held against Debtors' 5 acre parcel of land by Commtech Services, Inc., Mountain West Bank, the Montana Nursing Association, and Centron Services may be subject to avoidance. As a consequence, *Murdock* is not directly on point. *See Victor Gruen Associates v. Glass*, 338 F.2d at 829.

In *Murdock*, this Court construed the marshaling doctrine applying § 31-2-105. However, there is another Montana statute which governs marshaling, and specifically governs the order in which lienholders must resort to different funds, Mont. Code Ann. § 71-3-115:

> Where one has a lien upon several things and other persons have subordinate liens upon or interests in some but not all of the same things, the person having the prior lien, if he can do so without risk of loss to himself or of injustice to other persons, must resort to the property in the following order, on the demand of any party interested:
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> (1) to the things upon which he has an exclusive lien;
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> (2) to the things which are subject to the fewest subordinate liens;
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> (3) in like manner inversely to the number of subordinate liens upon the same thing; and

> (4) when several things are within one of the foregoing classes and subject to the same number of liens, resort must be had:
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> (a) first, to the things which have not been transferred since the prior lien was created;
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> (b) second, to the things which have been so transferred without a valuable consideration; and
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> (c) third, to the things which have been so transferred for a valuable consideration in the inverse order of the transfer.

See Sisters of Charity of Providence of Montana v. Nichols, 157 Mont. 106, 114, 483 P.2d 279, 284 (1971).

Both sections 31-2-105 and 71-3-115 address marshaling principles and both contain restrictions where marshaling would involve the risk of injustice to other persons. *In re Martin*, 875 P.2d 417, 420-21 (Okl. 1994); *see also Hill v. Lane*, 848 P.2d 43, 44-45 (Okl. App. 1992). Marshaling of assets may not be performed if it cannot be performed without injustice to third persons. *Murdock*, 134 B.R. at 423, 10 Mont. B.R. at 187-88; *Martin*, 875 P.2d at 420, 422; *Hill v. Lane*, 848 P.2d at 45. There are numerous liens in this case, two assets, and marshaling, if imposed, would follow the more specific statute addressing marshaling involving lienholders under § 71-3-115.

Section 71-3-115 would require Wells Fargo Bank to resort to the things which are subject to the fewest subordinate liens. First, the record does not support Debtors' assertion that Wells Fargo Bank has an exclusive lien on Debtors' homestead property. To the contrary, it appears that several creditors, including Mountain West Bank, have liens against the 5 acre parcel. Moreover, under Debtors' proposed distribution, Mountain West Bank stands to receive payment in full on its consensual lien, which was converted to a judgment lien, ahead of the first

consensual lienholder, Wells Fargo Bank.[5] Such proposed distribution smacks of inequity and as noted in *In re Frazier*, 17 Mont. B.R at 259, marshaling is an equitable doctrine.

Second, it is not at all clear whether Debtors' homestead property is encumbered by fewer subordinate lienholders, although the Court suspicions that Debtors homestead property is encumbered by equally as many creditors. Therefore, Debtors have not satisfied the second prong of Mont. Code Ann. § 71-3-115.

Finally, not one of the parties in interest has provided the Court with a closing statement reflecting the real estate commission and closing fees that were or will be subtracted from the sales price of $115,000. Additionally, Debtors' counsel made a passing comment that he wanted to work something out with the Trustee on his fee, but after all is said and done, it does not appear that Debtors would have enough proceeds from the sale to make the distributions provided for in their Amended Motion filed December 1, 2005, this is so even with the gracious reduction by Mountain West Bank of its claim to $70,000.

Given the unanswered questions and the appearance of inequity, this Court cannot approve Debtors' proposed distribution. In this case, the proceeds of the sale must be distributed in order of priority. As such, the proceeds must go to Wells Fargo Bank. According to the appraisal done by James R. Campbell on behalf of Mountain West Bank, the consensual lien held by Mountain West Bank is adequately protected by the value of Debtors' residence. The Court's ruling is more particularly warranted in this case where one could argue that Debtors' sale masquerades as a plan which defeats the protections afforded to creditors by

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[5] Debtors' amended their Motion on December 1, 2005, to properly reflect Commtech Services, Inc. and property taxes of $466.52 owing to Broadwater County.

Chapter 13 of the Bankruptcy Code.

II. Motion to Approve Sale of Silos Inn Held December 15, 2005

On December 20, 2005, Debtors, through attorney Lewis K. Smith, filed a Motion seeking approval by the Court of a sale of Debtors' business property, referred to as the Silos Inn, which property was sold by auction held pursuant to an approved agreement between Debtors and Gateway Economic Development Corporation. Interestingly, on December 22, 2005, Debtors, through attorney Gregory W. Duncan, objected to their own Motion to Approve Sale of Silos Inn Held December 15, 2005. Debtors' objection to approval of the sale is two-fold. First, Debtors assert that sufficient notice of the auction was not provided to the general public. Second, Debtors maintain that private discussions between two of the bidders, namely Rod Grover and Lewis Reeves, the successful bidder at the December 15, 2005, auction, create the appearance of collusion.

Gateway Economic Development Corporation is a secured creditor with a first lien position in the Silos Inn property. Debtors and Gateway Economic Development Corporation entered into a Stipulation that was filed with the Court on November 11, 2005. The Stipulation resolved matters then pending in Adversary Proceeding 05/00055. The Stipulation, approved by Order of this Court entered November 14, 2005, provides:

> 1. The Debtors shall be allowed to advertise and sell the Silos Inn real property in Broadwater County until December 10, 2005. The sale will be for cash at closing, and include all of the Silos Inn property in one sale. If an acceptable buy-sell agreement has not been completed by December 10, 2005, the parties shall proceed to sell the property as a whole at public auction on or before December 15, 2005.

* * *

> 2. Gateway agrees to provide Debtor's [sic] counsel a key, upon the execution of this agreement, to allow him to show the property. . . Gateway shall continue to pay the insurance and power bills for the property. Counsel for Debtors shall photograph the premises upon first entering after receiving the key. Counsel agrees that he will not give the key to the Debtors and will not duplicate the key.
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> 3. Gateway agrees that the value of its claim shall be the sum of $230,000.00. Gateway agrees to continue to pay the power bills and insurance on the property through closing, for which it shall be reimbursed for funds expended after November 10, 2005, at closing.

Debtors were not successful in the sale of the property and thus began taking steps around December 10, 2005, or shortly thereafter, to proceed with an auction of the Silos Inn property on December 15, 2005. Specifically, Debtors' counsel contacted via telephone some interested parties, left voice mail messages for other interested parties and published Notices of the sale in the Independent Record on December 14 and 15, 2005, and in the Great Falls Tribune on December 13, 14 and 15, 2005. The auction was conducted in Helena, Montana on December 15, 2005. Two bidders, Mike Segota and Philip Land, participated in the auction by telephone. Other persons attending were: Lewis Reeves, Gregory Duncan and Lewis Smith (Debtors' counsel), Rod Grover, Bob Fusie, Dale Reagor (Gateway Economic Development Corporation's counsel), and Mountain West Bank's counsel. In accordance with the agreement between Debtors and Gateway Economic Development Corporation, bidding commenced at $230,102. The bidding went as follows:

$232,500 - Mike Segota

$235,000 - Lewis Reeves

$250,000 - Mike Segota

$252,500 - Lewis Reeves

$255,000 - Mike Segota

$257,500 - Lewis Reeves

$260,000 - Mike Segota

$262,500 - Lewis Reeves

$265,000 - Mike Segota

$270,000 - Lewis Reeves

$275,000 - Mike Segota

Following the foregoing bids, Mike Segota was pronounced the winning bidder with a bid of $275,000. Pursuant to the Notice of Public Auction, all bidders were required to give a letter of credit or present certified funds in a sufficient amount to cover the bidders' bids. Immediately following the conclusion of the bidding, it came to light that Mike Segota was not in possession of a letter of credit and would not be able to obtain a letter of credit until December 16, 2005, or shortly thereafter.

The closest bid to Mike Segota's bid was that of Lewis Reeves in the sum of $270,000 and Lewis Reeves presented a letter of credit. However, given the discovery that Mike Segota was not a qualified bidder, it was determined that all of his bids should be thrown out, leaving Lewis Reeves with the sole bid of $235,000. Rod Grover then indicated that he had a cashier's check in the sum of $250,000 and was willing to bid that amount. Lewis Reeves and Rod Grover then requested a recess and retired to an adjoining office. When they returned, Rod Grover withdrew from the bidding process and left. Lewis Reeves was then declared the successful bidder at $235,000. Counsel for Debtors (Gregory Duncan) and counsel for Mountain West Bank voiced their objections to the events of the auction and the parties

disbursed.

To further compound the problems associated with the auction, sometime after the auction but prior to the hearing date, a water pipe broke at the Silos Inn causing extensive water damage to the property. Counsel for Lewis Reeves appeared at the hearing and indicated that his client was willing to proceed with the sale. However, it was not clear whether Lewis Reeves would proceed with the sale "as is" or whether Lewis Reeves would seek an offset for the water damage. The Court is deeply troubled by the damage that has occurred to the Silos Inn property while under the control of Gateway Economic Development Corporation. The damage has undoubtedly reduced the value of the property and the Court is inclined to treat the damage as an offset against Gateway Economic Development Corporation's claim. However, the Court will not definitively decide the offset issue until further hearing to be held February 22, 2006. Prior to the February 22, 2006, hearing, Gateway Economic Development Corporation shall either have the damage repaired or obtain at least 2 bids from qualified licensed contractors on the cost of repairing the damage.

As for the sale, the uncertainty surrounding the intent of Lewis Reeves in light of the recent water damage, coupled with the disqualification of Mike Segota after the bidding process, rather than prior to the bidding process, the suggestion of collusion between Rod Grover and Lewis Reeves and the fact that notice of the sale was not published until just 2 days prior to the sale convinces this Court that the December 15, 2005, auction was seriously flawed and must be re-conducted.

While the Court is generally inclined to enforce the terms of an approved Stipulation, in this case, it is quite obvious that neither Debtors nor Gateway Economic Development

Corporation fully appreciated the difficulties created by the deadline for Debtors to sell the property and the deadline for an auction. The 5 day period between December 10, 2005, and December 15, 2005, did not leave the parties sufficient time to conduct an auction of the property, unless of course Gateway Economic Development Corporation would have taken steps to begin posting notices of the auction at the time the Stipulation was approved with the thought that the auction could be cancelled at the last minute if Debtors were successful in selling the property.

Several statutes require certain notice periods before a forced sale or auction shall occur. Mont. Code Ann. § 71-1-224 provides under mortgage law that "[r]eal estate sold under a power of sale given and contained in a mortgage of real estate . . . shall be advertised for sale at least 30 days before the date fixed for such sale[.]" Similarly, under the Small Tract Financing Act of Montana, at least a 120-day notice is required with "[a] copy of the notice of sale [being] published in a newspaper of general circulation published in any county in which the property or some part thereof is situated, at least once each week for 3 successive weeks . . . with the last publication . . . [being] at least 20 days before the date [of sale]." Mont. Code Ann § 71-1-315(1)(c). Mont. Code Ann. § 25-13-701(1)(c) requires at least 20 days notice for judgment execution sales. Mont. Code Ann. § 30-9A-612 requires at least 10 days notification prior to a sale conducted under Article 9A of the Uniform Commercial Code. The one day notice provided in the Independent Record and the two days notice in the Great Falls Tribune (the Court is excluding the notices which ran in the above newspapers on the day of the sale) were insufficient given the notice requirements contained in other forced sale or auction provisions provided under Montana law.

For the reasons discussed above, the Court concludes that the auction should be re-conducted, with proper notice given to parties in interest and the general public. The new auction shall be held on Wednesday, February 22, 2006, at 1:00 p.m. in the 2ND FLOOR COURTROOM, FEDERAL BUILDING, 400 N. MAIN, BUTTE, MONTANA. I will be available for questions during the auction and immediately following the auction, and reserve the right to conduct the auction if any issues arise at the scheduled sale time. All prospective bidders must satisfy prior to the commencement of the sale that they have the requisite bidding credentials, i.e., cash, irrevocable letter of credit, or certified funds satisfactory to the auctioneer or to the Court to pay any awarded bid made by the successful bidder after all other bidders are closed out of the auction. At 2:00 p.m., I will conduct a hearing on (1) approval of the sale by auction, including whether the sale meets all the requirements of 11 U.S.C. § 363, including the good faith requirements of § 363(m); and (2) on the offset, if any, that should be charged against Gateway Economic Development Corporation's claim for the damages that have resulted to the Silos Inn property while under the exclusive control of Gateway Economic Development Corporation. Consistent the with foregoing, the Court will enter a separate order that provides as follows:

IT IS ORDERED:

1. The objections filed by Wells Fargo Bank, N.A. on December 11, 2005 (Dkt. 124), and January 9, 2006 (Dkt. 169), and the Chapter 13 Trustee on December 29, 2005 (Dkt. 147), are SUSTAINED; and Debtors' "Motion for Approval of Distribution of Proceeds from Sale of 8 Acres" (Dkt. 117) filed December 1, 2005, as superseded by Debtors' "Amended Motion for Approval of Distribution of Proceeds from Sale of 8 Acres" filed December 29, 2005 (Dkt. 150),

is DENIED.

2. The objections filed by attorney Gregory W. Duncan on behalf of Debtors (Dkt. 137 and 140), Mountain West Bank (Dkt.142) on December 22, 2005, and the Chapter 13 Trustee on December 29, 2005 (Dkt. 148) are SUSTAINED; and the "Motion to Approve Sale of Silos Inn Held December 15, 2005" (Dkt. 130) filed by attorney Lewis K. Smith on behalf of Debtors on December 20, 2005, is DENIED.

3. Debtors and Gateway Economic Development Corporation shall re-notice the auction of Debtors' property referred to as the Silos Inn property, in accordance with applicable Montana law, for **Wednesday, February 22, 2006, at 1:00 p.m. in the 2ND FLOOR COURTROOM, FEDERAL BUILDING, 400 N. MAIN, BUTTE, MONTANA**. Attorney Lewis K. Smith will be in charge of conducting the auction.

4. A hearing on approval of the Silos Inn property, including whether the sale meets all the requirements of 11 U.S.C. § 363, and a hearing on the extent of the damage caused by water to the Silos Inn property and the responsibility therefore, shall be held **Wednesday, February 22, 2006, at 2:00 p.m. in the 2ND FLOOR COURTROOM, FEDERAL BUILDING, 400 N. MAIN, BUTTE, MONTANA**.

BY THE COURT

HON. RALPH B. KIRSCHER
U.S. Bankruptcy Judge
United States Bankruptcy Court
District of Montana